



**COUNTY OF LOS ANGELES
DEPARTMENT OF AUDITOR-CONTROLLER**

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April 8, 2009

TO: Supervisor Don Knabe, Chairman
Supervisor Gloria Molina
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Michael D. Antonovich

FROM:

Wendy L. Watanabe
Auditor-Controller

SUBJECT: **FISCAL REVIEW OF RITES OF PASSAGE RESIDENTIAL CENTER,
INCORPORATED - A GROUP HOME FOSTER CARE CONTRACTOR**

Attached is our report on the fiscal operations of Rites of Passage Residential Center, Incorporated (ROP or Agency) from January 1, through December 31, 2005. ROP was licensed to operate two group homes (GH), each with a resident capacity of six children. ROP was located in the Second Supervisorial District.

The Department of Children and Family Services (DCFS) and the Probation Department contracted with ROP to care for foster children placed in the Agency's homes. The County paid ROP \$4,858 per child per month, based on a rate determined by the California Department of Social Services. During calendar year 2005, the Agency received \$658,878 in GH foster care funds.

On March 2, 2007, ROP advised DCFS that they intended to close the group homes immediately and requested that DCFS remove all placed children. DCFS informed us all foster children were removed from the Agency on March 5, 2007. The State terminated ROP's foster care rate effective June 12, 2007 and the County allowed ROP's GH agreement to expire effective October 31, 2007.

Scope

The purpose of our review was to determine whether ROP complied with its contract terms and appropriately accounted for and spent foster care funds on allowable and reasonable expenditures. We also evaluated ROP's expenditure and revenue documentation, internal controls and compliance with applicable federal, State and County fiscal guidelines governing GH foster care funds.

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Summary of Findings

We identified \$7,354 in unallowable costs and \$148,192 in unsupported/inadequately supported costs. In addition, DCFS and the Agency need to work together to resolve some potential overpayments.

We also noted that ROP owes \$148,158 in delinquent federal payroll taxes. If DCFS considers contracting with ROP in the future, ROP management needs to submit a plan to DCFS on how they will pay the liability without using current period foster care funds. ROP also needs to ensure that its Board of Directors is independent. Finally, ROP needs to strengthen its internal controls over employee loans, accounting and disbursements, bank reconciliations, payroll/personnel records and payments to independent contractors. Details of our findings are discussed in the attached report.

We recommend that DCFS resolve the questioned costs and, to the extent possible, collect any disallowed amounts. In addition, if DCFS contracts with ROP in the future, DCFS needs to ensure that ROP's management takes action to address the recommendations in this report and monitor to ensure that the actions result in permanent changes.

Review of Report

We discussed our report with ROP's management on June 3, 2008. As previously noted, ROP no longer has a GH contract with the County. If the Agency submits a written response to DCFS, DCFS will incorporate the Agency's response into a Fiscal Corrective Action Plan that will be submitted directly to the Audit Committee. We thank ROP's management and staff for their cooperation during our review.

Please call me if you have any questions, or your staff may contact Jim Schneiderman at (213) 253-0101.

WLW:MMO:JLS:MWM

Attachment

c: William T Fujioka, Chief Executive Officer
Patricia S. Ploehn, Director, Department of Children and Family Services
Ted Myers, Chief Deputy Director, Department of Children and Family Services
Susan Kerr, Senior Deputy Director, Department of Children and Family Services
Robert B. Taylor, Chief Probation Officer
Turesi Faniel, Executive Director, Rites of Passage Residential Center
Board of Directors, Rites of Passage Residential Center
Cora Dixon, Bureau Chief, Foster Care Audits Bureau, CA Dept of Social Services
Commission for Children and Families
Public Information Office
Audit Committee

Rites of Passage Residential Center
Fiscal Review

REVIEW OF EXPENDITURES/REVENUES

We identified \$7,354 in unallowable costs and \$148,192 in unsupported/inadequately supported costs. In addition, DCFS and ROP need to work together to resolve some potential overpayments. Details of these costs/overpayments are discussed below.

Applicable Regulations and Guidelines

ROP was required to operate its GH in accordance with the following federal, State and County regulations and guidelines:

- GH Contract, including Exhibit C-1, and the Auditor-Controller Contract Accounting and Administration Handbook (A-C Handbook)
- Federal Office of Management and Budget Circular A-122, Cost Principles for Non-Profit Organizations (Circular)
- California Department of Social Services Manual of Policies and Procedures (CDSS-MPP)
- California Code of Regulations, Title 22 (Title 22)

Unallowable Costs

We identified \$7,354 in unallowable expenditures:

- \$5,000 in foster care funds were used for delinquent federal payroll taxes due from September 1997 to December 2001. Using current period foster care funds to pay prior years' delinquent taxes is an unallowable use of funds.
- \$2,237 in interest and penalties consisting of \$1,132 in overdraft and non-sufficient fund bank fees, \$977 in late payment fees and \$128 in finance charges. Interest and penalties are not allowable according to Circular A-122, Sections 16 and 23.
- \$117 in personal expenditures, involving adult entertainment cable television charges. A-C Handbook Section 1.5 states that only expenditures that are necessary, proper and reasonable to carry out program purposes and activities are allowable.

Unsupported/Inadequately Supported Costs

A-C Handbook Section A.3.2 states that all expenditures shall be supported by original vouchers, invoices, receipts, or other supporting documents, and that unsupported expenditures will be disallowed upon audit. Photocopied invoices or receipts, any internally generated documents (i.e., vouchers, request for check forms, requisitions, canceled checks, etc.) and account statements do not constitute supporting documentation for purchases.

We identified \$148,192 in expenditures that were either unsupported, or were inadequately supported. Specifically:

- \$87,286 in unsupported salary expenditures to the Assistant Executive Director and the Group Home Administrator. ROP did not provide time sheets for either individual. A-C Handbook Section B.3.1 states that time cards or time reports must be prepared for each pay period. We also noted that there was no personnel file for the Group Home Administrator.
- \$23,397 in inadequately supported expenditures to an independent contractor. The Agency provided a contract but did not have any invoices or other documentation detailing the work performed or the rate paid to this contractor.
- \$17,985 in inadequately supported expenditures on credit cards and gasoline credit cards, food, supplies and payments to the facility manager. The Agency provided credit card statements and cancelled checks, but did not provide original itemized receipts or an explanation of the expenses.
- \$11,612 in inadequately supported vehicle lease payments, insurance and DMV license renewal for a 2005 Lincoln Navigator used by the Executive Director. ROP did not maintain mileage logs, or other documentation showing this vehicle benefited the group home children. ROP did maintain mileage logs for two other Agency vehicles (one for each group home) documenting the business use of these vehicles. In addition to the inadequately supported costs of the Lincoln Navigator, this luxury vehicle may not have been an appropriate choice for the Executive Director's vehicle. A-C Handbook Section C.1.5 states that only expenditures that are necessary, proper and reasonable to carry out the purposes and activities of the Program are allowable. Using a Lincoln Navigator does not appear to be necessary, proper or reasonable.
- \$5,185 in building repairs, independent contractor expenditures and uncategorized expenses for which the Agency had no other documentation. Without receipts, invoices, or other documentation, we could not determine if these expenditures were program related.

- \$2,727 in inadequately supported petty cash expenditures. ROP recorded these expenditures on a petty cash log. However, ROP did not provide receipts for the majority of these expenditures. The receipts that were provided did not identify the purpose of the expenditure or for whom the purchase was made. Therefore, we were unable to determine if the expenditures benefited the group home children.

Recommendations

1. DCFS management resolve the \$155,546 (\$7,354 + \$148,192) in questioned costs and collect any disallowed amounts.

If DCFS considers contracting with ROP in the future, ROP management:

2. Comply with required supporting documentation for all expenditures, including time sheets, mileage logs, and original itemized invoices and receipts, and all other contract documentation requirements.
3. Ensure that foster care funds are used for allowable expenditures to carry out the purpose and activities of the Agency's programs.

Potential DCFS Overpayments

DCFS' records show some potential overpayments made to the Agency. DCFS and the Agency should work together to resolve the overpayments, and DCFS should collect any verified overpayments. ROP's management should ensure that any future payment discrepancies are immediately reported to DCFS and any excess amounts are repaid promptly.

Recommendations

4. DCFS management work with ROP to resolve the overpayments and collect any verified overpayments.
5. If DCFS considers contracting with ROP in the future, ROP management ensure that any payment discrepancies are immediately reported to DCFS and any excess amounts are repaid promptly.

CONTRACT COMPLIANCE AND INTERNAL CONTROLS

We noted several contract compliance issues and internal control weaknesses. If DCFS contracts again with ROP, DCFS should ensure that ROP management takes action to address the recommendations in this report. DCFS should also monitor to ensure the actions result in permanent changes.

Payroll Tax Liability

ROP owes \$148,158 in delinquent federal payroll taxes, penalties and interest from September 30, 1997 to December 31, 2001.

ROP's internally generated, unaudited December 31, 2005 balance sheet shows negative net assets of \$288,245. In addition, it appears that ROP had cash flow problems and had to obtain numerous loans from the Executive Director (see section on Loans from the Executive Director). Because ROP has no net assets, the Agency may have used current period foster care contract funds to pay its delinquent tax liability, which is not an allowable use of these funds.

As previously indicated, the Agency closed its group homes and all County placed children were removed. If DCFS decides to contract with ROP in the future, ROP management needs to submit a plan to DCFS describing how they will pay their federal payroll tax liability without using current period foster care funds. In addition, we noted that the IRS liability was not recorded on ROP's balance sheet.

Recommendations

6. **DCFS management ensure that current foster care funds are not used to pay penalties and interest to the IRS.**

If DCFS considers contracting with ROP in the future, ROP management:

7. **Submit a plan to DCFS on how the Agency will pay its IRS liability without using current period funds and record the IRS liability on the Agency's balance sheet.**
8. **Determine if ROP used foster payment contract funds to pay its delinquent tax liability and attempt to recoup these funds.**

Board of Directors Independence

California Corporations Code Section 5227 states that not more than 49% of the persons serving on the board of any corporation may be "interested persons." "Interested persons" include persons currently being paid by the corporation for services rendered to it within the previous 12 months. Five of the seven ROP Board members (71%) are either compensated by the Agency or are related to an employee of the Agency. Specifically, the Agency's Assistant Executive Director, Program Manager and Therapist serve on ROP's Board and also received a salary from the Agency. Two other Board members have children who are employees of the Agency.

Recommendation

- 9. ROP management must ensure that the membership of the Agency's Board of Directors complies with the California Corporations Code.**

Board Minutes

California Corporations Code Section 6320 requires corporations to keep minutes of their board meetings. ROP did not provide the 2005 Board minutes for our review. Therefore, we were unable to confirm if the Agency prepared Board minutes as required by the State Corporations Code.

Recommendation

- 10. If DCFS considers contracting with ROP in the future, ROP management ensure that minutes are kept for each Board of Directors meeting.**

Loans from the Executive Director

During our review period, the Executive Director made seven loans totaling \$79,185 to the Agency. We verified that the loan proceeds were deposited into the Agency's bank accounts. However, the Agency did not provide written loan agreements.

A-C Handbook Section A.3.2 requires the Agency to establish a written loan agreement between the Agency and its employees to document all loans.

Recommendation

- 11. If DCFS considers contracting with ROP in the future, ROP management establish written agreements for all loans, indicating the amount of the loan and repayment terms.**

Accounting and Disbursement Procedures

We noted the following weaknesses in the Agency's accounting and disbursement procedures:

- Eight expenditures totaling \$9,764 were not properly classified in the Agency's general ledger. For example, we noted several expense items that were listed as "uncategorized expense." A-C Handbook Section A.2.5 states that each account title must clearly identify the nature of the transaction(s) posted to the account.

- Eighty-three petty cash disbursements, totaling \$1,238, were not recorded in the general ledger. We also noted 29 credit card charges, totaling \$1,948, that were not recorded on the general ledger.
- Four checks totaling \$6,340 were made payable to "Cash." A-C Handbook Section B.2.1 states that checks shall not be payable to cash.
- The check signer and payee was the same employee on 40 checks totaling \$26,444. Most of the checks were for petty cash. A-C Handbook Section B.2.2 states that a second signature is required on all checks where the check signer and the payee are the same employee.
- The Agency did not provide a fixed assets listing. Therefore, we could not confirm if a listing was prepared. A-C Handbook Section B.4.2 states that contractors should maintain a current listing of fixed assets, including the item description, serial number, date of purchase, acquisition cost and sources of funding. In addition, the A-C Handbook states that fixed assets be appropriately tagged and inventoried annually to ensure that they are accounted for and maintained in proper working order.

Recommendations

If DCFS considers contracting with ROP in the future, ROP management:

- 12. Ensure all expenditures are properly recorded in the Agency's general ledger.**
- 13. Ensure that checks are not made payable to "Cash."**
- 14. Require two signatures on all checks where the payee and the check signer are the same employee.**
- 15. Maintain a fixed asset listing and conduct an inventory of fixed assets at least yearly to ensure that all fixed assets are accounted for and maintained in proper working order.**

Bank Reconciliations

A-C Handbook Section 1.4 states that monthly bank reconciliations should be prepared within 30 days of the bank statement date and management review the reconciliation for appropriateness and accuracy. Both the preparer and the reviewer should sign and date the bank reconciliations. At ROP, the preparer did not sign/date the bank reconciliations, and management did not review the reconciliations. Also, six checks from 2002, totaling \$2,708, and six checks from 2004, totaling \$4,535, were still outstanding.

Recommendations

If DCFS considers contracting with ROP in the future, ROP management:

16. Ensure the Agency's bank account reconciliations are signed and dated by both the preparer and the reviewer, and reviewed by management for appropriateness and accuracy.
17. Review and cancel any checks that have not been negotiated within six months and reissue, if appropriate.

Payroll/Personnel Controls

CDSS-MPP Section 11- 402 requires that supporting documentation be maintained for all program expenditures, including employee salary rates. A-C Handbook Section B.3.1 states that timecards or time reports must be prepared for each pay period, and the employee and the employee's supervisor certify the accuracy of the reported time. Also, the employee and supervisor must sign the timecard in ink.

We sampled the personnel files and payroll records of 12 employees and noted the following:

- Three employees did not prepare timecards or time sheets.
- Six time sheets did not have a supervisor's signature.
- None of the employees' personnel files had a salary rate sheet or the rate on file was not current.
- One personnel file was not available for our review.

Recommendations

If DCFS considers contracting with ROP in the future, ROP management:

18. Ensure employee timecards are prepared for each pay period and the employee and the employee's supervisor certify the accuracy of the reported time. Also, ensure the employee and supervisor sign the timecard in ink.
19. Ensure employee salary rates are consistently documented and updated in the employee's personnel file.
20. Ensure personnel files are maintained for each employee.

Independent Contractors

A-C Handbook Section A.3.2 on Consultant Services requires agencies to have a contract, time and attendance records, billing rates and invoices for contractors. We reviewed five independent contractors ROP hired and noted:

- Three contractors did not have current contracts with the Agency.
- Two contractors were not issued 1099 Forms by the Agency to report payments to the taxing agencies.
- Three independent contractors did not provide invoices.
- One independent contractor's income recorded on the Agency's general ledger was more than the amount reported on the 1099.

Recommendations

If DCFS considers contracting with ROP in the future, ROP management:

- 21. Ensure the Agency has a contract with billing rates for each contractor.**
- 22. Ensure the Agency maintains supporting documentation for all independent contractors, including contracts and invoices.**
- 23. Ensure that all payments to independent contractors are properly reported to the federal and State taxing agencies.**